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Memorandum to Members of the Wyoming Blockchain Task Force

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### **Digital Asset Categories**

We would like to commend the Wyoming legislature and the members of the Wyoming Blockchain Task Force on their forward-looking and supportive stance in respect of blockchain technology. We believe the legislation adopted to date helps to clarify the landscape and provide direction for the development and issuance of blockchain tokens and other digital assets.

We note that recently enacted laws in Wyoming describe and define three types of digital assets: (i) digital consumer assets, (ii) digital securities, and (iii) virtual currency. We would propose that the Wyoming legislature consider an additional category of digital assets—digital pass-through assets. Such a category would address the treatment of digital assets that merely represent an ownership interest in some other underlying asset, such as a physical commodity.

This pass-through category should be applied in circumstances where the digital asset represents, and is backed on a one-for-one basis by, the relevant underlying physical asset and the owner of the digital asset has an absolute right to obtain the title to, and ownership and possession of, the underlying asset. In such circumstances, the digital asset is merely a digital method for evidencing ownership of the underlying physical asset. As such, the digital asset should be classified for commodities law and other purposes as the equivalent of the underlying physical asset.

Taking another current real-world example, eCertificates issued by banks or brokerage firms are one accepted method for investing in certain physical commodities, including certain precious metals, base metals and agricultural commodities. Each eCertificate represents a specified quantity of the underlying commodity. They are held electronically through a brokerage or similar account and can be purchased and sold without the need for the individual holder to take physical possession of, and transport, the underlying physical commodity. In summary, they

provide the benefits (and costs) of ownership without the burdens of transporting and storing the underlying assets. Instead, those underlying assets are held in the name of, and stored on behalf of, the issuer of the eCertificates. From a legal and regulatory perspective, the holder of the eCertificate is generally viewed as holding an interest in the specified amount of the underlying physical commodity.

Failing to establish a category specific to digital pass-through assets may have unintended consequences. For example, in the absence of other legislation or guidance, digital pass-through assets might be grouped together with digital consumer assets under the Wyoming law passed this year, as this is the catch-all category used for digital assets that do not fall within the definition of digital security or virtual currency. Digital pass-through assets (other than digital pass-through assets whose underlying assets are shares or other securities) should not be classified as securities, as the underlying asset is not a security and there is nothing about the digital pass-through asset that suggests that it should be treated as an investment contract or other type of security (i.e., there is no investment in a common enterprise with an expectation of profit from the efforts of others). However, in the absence of a clear category for digital pass-through assets, there is some risk that a regulator or judge might take the view that they should be classified as digital securities. Although, in theory, a digital pass-through asset might be used as a medium of exchange, that is not the primary purpose of digitizing the asset and the underlying physical asset to which the digital asset is tied may not have the pricing stability to support its use as a medium of exchange. That leaves the digital consumer asset category as the fallback classification even though the asset is not typically used for consumptive, personal or household purposes.

Based on the above, we believe it is best to treat digital pass-through assets as a separate category. They would basically be the equivalent of eCertificates and the laws applicable to the underlying assets would be applied to such digital assets to the extent appropriate. For example, a digital asset representing an amount of gold bullion stored in a bank vault or warehouse would be treated as gold bullion, and securities laws would not apply to such digital asset. Certain conditions would need to be established in order to support such treatment. For example, there would need to be evidence that the corresponding amount of gold bullion is, in fact, stored at a bank or other warehouse. In addition, the holder of the digital pass-through asset must have an absolute right to redeem the digital asset for the corresponding amount of gold bullion.

Although the above discussion has focused on digital pass-through assets relating to physical commodities, digital pass-through asset categorization may be appropriate in certain other situations as well. For example, although there has been some controversy around so-called stable coins and the extent to which reserves for such coins are maintained on a one-for-one basis, it may be appropriate to treat true fiat-

backed stable coins (i.e., stable coins that are backed one-for-one by documented reserves maintained in the underlying fiat currency and which may be redeemed at substantially any time for an equivalent amount of the underlying fiat currency) as a type of digital pass-through asset.

We recognize that there may be differences in certain situations between the treatment of a physical asset and the digital representation of such asset. For example, creating and perfecting a security interest in physical gold bullion may be appropriate through filing when the gold bullion is actually possessed by its owner. Perfection of a security interest in a gold-backed digital asset, on the other hand, may be appropriate through some concept of account control. Thus, the legal treatment of this type of digital asset will need to be fully considered as part of the legislative process.

We also note for the Task Force's consideration that there may be other types of digital assets that do not meet the criteria described above for digital pass-through assets and do not otherwise easily fit within any of the other existing categories for digital assets under the Wyoming law (putting aside the catch-all language incorporated in the definition of digital consumer assets). For example, consider a commodity-backed digital asset that allows the issuer to satisfy a redemption request in cash (i.e., the value of the underlying gold at the time of redemption) rather than by transfer of the physical asset. Such a digital asset would not satisfy the criteria discussed above for digital pass-through assets. But it would also not squarely fall within any other existing category of digital assets. In our view, it is not properly classified as a digital security, as there is no value being derived from the efforts of the issuer or any other common enterprise. Nor is it being used as a type of virtual currency or for any apparent consumer purpose. Although we recognize that there may be practical difficulties in doing so, we would recommend (possibly as a medium-term project) that the Task Force consider proposing a miscellaneous category of digital assets for those digital assets that do not comfortably fall within the existing categories. Perhaps these could be addressed on more of a case-by-case basis by designating a state agency with authority to review the characteristics of particular digital assets for which guidance is sought and to determine the appropriate category or treatment for such miscellaneous digital assets.

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Thank you for your consideration of the points raised in this memorandum. We would be happy to address any questions with the members of the Task Force and their colleagues.